NATIONAL COUNCIL OF STATE AGRICULTURAL FINANCE PROGRAMS

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FARM CREDIT ADMINISTRATION HEARINGS
Financing Young, Beginning and Small Farmers and Ranchers
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David Wirth, Steering Committee Chair
Dwirth@mail.state.il.us 217/782-5792

NATIONAL COUNCIL OF STATE AGRICULTURAL FINANCE PROGRAMS
Good Afternoon, Chairman Reyna, Ms. Jorgenson and Mr. Flory. My name is David Wirth. I am the Executive Director of the Illinois Farm Development Authority (IFDA). I also serve as the Steering Committee Chair for the National Council of State Agricultural Finance Programs (NCOSAFP). I am here representing NCOSAFP today. The National Council of State Agricultural Finance Programs has 26 member states, each of which offers one or more state sponsored financing programs for farmers and/or agri-businesses. Each of these financing programs provides benefits to the borrowers and to the lenders that participate with the programs. Many of the financing programs offered by our members are targeted to young, beginning and small farmers and ranchers.

TYPICAL STATE SPONSORED AGRICULTURAL FINANCE PROGRAMS
Typical state sponsored agricultural financing programs offered by NCOSAFP members include loan participations, state loan guarantees, agricultural (aggie) bonds and direct loans. The loan participations often involve commercial lenders who have first lien positions and the state agency finances a portion of the debt with second lien positions. The state loan guarantees are used by commercial lenders to guarantee a percentage of a loan. Agricultural (aggie) bonds are federally tax exempt and allow commercial lenders an opportunity to offer reduced rate financing to young farmers and ranchers. In addition, some of the NCOSAFP members offer direct loans and some of those direct loans use loan guarantees from USDA's Farm Service Agency.

COMMEND FCA EFFORTS TO IMPROVE YBS FINANCING
I commend the Farm Credit Administration's efforts to improve young, beginning and small (YBS) farmer and rancher financing. Clearly, young farmers and ranchers represent agriculture's future. There are many opportunities for Farm Credit institutions across the country to better serve YBS farmers and ranchers by working with state agricultural financing agencies. The various programs that are offered for YBS farmers, such as loan participations and loan guarantees can be used by Farm Credit Services. The programs can enhance credit quality, improve loan terms and allow the FCS institutions to more readily serve the needs of young, beginning and small farmers and ranchers.

ANECDOTAL EVIDENCE
At this time, I would like to share some anecdotal evidence. A young farmer, whom I will call "Tom", was starting farming. He contacted his local Farm Credit Services and became a Farm Credit Services customer. Another young farmer, "Mike", started farming, contacted his local Farm Credit Services office and was sent to the local bank. Tom and Mike represent actual individuals with similar financial positions and experience. The primary difference between these two examples is timing. Tom approached Farm Credit in 1982 or 1983, while Mike began his career in 2001 or 2002. In my opinion, the difference in the FCS lender's response represents a fundamental change in philosophy. I

spoke with a Farm Credit loan officer who told me that his credit committee discouraged him from doing small, unseasoned loans. This illustration may be an isolated case and might not be representative of the Farm Credit Services throughout the country. Unfortunately, I have reason to believe that this is becoming the norm and improvements in service to YBS farmers and ranchers are needed.

CONFLICTING MUTUALLY EXCLUSIVE OBJECTIVES?

It is possible that Farm Credit Services has conflicting, mutually exclusive objectives. That is to say the safety, soundness and profitability objectives may be in conflict with the objective of serving YBS farmers and ranchers. Often, YBS farmer loans are not seasoned. They are typically smaller than average and represent higher credit risk than seasoned loans from well-established farmers. To mitigate this higher risk, Farm Credit Services could make more use of the special programs that are offered in many states by members of the National Council of State Agricultural Finance Programs and programs offered by USDA's Farm Service Agency. Many of these financing programs can improve loan terms and reduce risk, thus allowing Farm Credit Services to safely and appropriately serve YBS farmers and ranchers. It is also my observation that volume-based compensation can lead a rational loan officer to direct his or her efforts to larger, more well-established farmers rather than taking the extra time required to do smaller loans for YBS farmers. My point is not to speak against commissions for loan volume. In fact, it can be a very good compensation mechanism. I simply wish to illustrate that volume-based compensation that does not differentiate between YBS loans and "standard" loans can create an additional conflict that may discourage efforts to finance YBS farmers and ranchers.

AGGIE BONDS

Allow me to take a few moments to explain agricultural (aggie) bonds. Aggie bond programs are one of the common threads among several NCOSAFP members. Aggie bonds help lenders provide reduced interest rate financing for young farmers' first-time farmland purchases and also for purchases of certain depreciable assets. The income from an aggie bond is federally tax exempt to the lender. Aggie bonds are not useful for Farm Credit Services Federal Land Bank institutions because Federal Land Bank's income is already tax exempt. However, aggie bonds might be useful for FCS Production Credit Associations for use with machinery, equipment and building loans. The tax advantage offered to the Production Credit Association could allow the PCA's to offer reduced interest rates for YBS purchases of certain classes of depreciable property.

SUCCESSES

There are many instances of successes where Farm Credit Services participates with state-sponsored agricultural finance programs. For example, in Illinois, First Farm Credit Services is active with Illinois Farm Development Authority's State Loan Guarantee Programs. In North Carolina, Farm Credit Services has been participating with the North Carolina Agricultural Finance Authority and their Ag-Start Program. In California, Farm Credit Services is active with Cal Coastal in an advisory role and also in making referrals. There are other NCOSAFP member states that have active participation with Farm Credit Services as well.

OPPORTUNITITES

There are many opportunities for Farm Credit Services to better serve more YBS farmers and ranchers by working with state agricultural finance agencies and programs. Additionally, the USDA Farm Service Agency offers several YBS farmer and rancher programs that can be very useful to Farm Credit Services and its constituents. There might also be opportunities to work in individual states to improve existing state-sponsored agricultural finance programs or to develop new programs that may be helpful for serving YBS farmers and ranchers.

Lenders should not simply look at the value or the profit from one YBS farmers' loan, but rather focus on the long-term value of the relationship and the series of loans and financial transactions that may take place over a lifetime. FCS has an opportunity to develop a longer-term view of the relationship value of YBS farmers and ranchers.

QUANTIFIABLE

Farm Credit Services' use of special state-sponsored financing programs for YBS farmers and ranchers can be rather easily quantified. For example, in a given state, Farm Credit Services' agricultural loan market share can be easily compared with the market share held by commercial banks. Similarly, the respective share of state-sponsored finance program activity between Farm Credit Services and commercial banks can be compared. If FCS is utilizing state-sponsored programs for YBS, there should be some parallels between the FCS agricultural loan market share and their share of the state-sponsored YBS farmers and ranchers programs. This comparison could be done with state-sponsored programs as well as with federally sponsored programs offered through the USDA's Farm Service Agency. Naturally, aggie bond financing of farmland purchases should be excluded from the calculations, since the tax exemption offered through aggie bonds does not benefit Federal Land Bank institutions.

When measuring loan activity to YBS farmers and ranchers, each should be counted in only one of the three young, beginning or small categories. Further, lending activity to YBS farmers and ranchers should be tracked by individual borrower, not by multiple loans to one borrower.

THANK YOU

On behalf of the National Council of State Agricultural Finance Programs, I thank you for the opportunity to participate in this forum. I look forward to continuing opportunities to work together with the Farm Credit System to provide constructive financing to young, beginning and small farmers and ranchers.

David Wirth was raised on a family farm in northern Illinois. He holds a bachelor's degree in agricultural economics from the University of Illinois. Work experience with the Farm Credit System includes five years as a branch office manager for the Bloomington (Illinois) Production Credit Association and participation in the Federal Land Bank's summer intern program.

He is the Executive Director of the Illinois Farm Development Authority, a state agency that offers credit enhancement programs to Illinois farmers.

David is the Steering Committee Chair for the National Council of State Agricultural Finance Programs (NCOSAFP) and serves as a member of the USDA advisory committee on beginning farmers and ranchers.